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SUBJECT: THE CHALLENGES OF INVESTING IN MOLDOVA

Classified By: Ambassador Michael D. Kirby for reasons 1.4 (b) and (d)

¶11. (C) SUMMARY: Although the Government of Moldova (GOM) has adopted measures to attract foreign investment, the business climate remains uneven. In 2006, Moldova achieved record foreign direct investment (FDI) of USD 240 million and 2007 continues to show a positive trend. However, FDI inflows remain low in relative terms and reports from foreign investors document the continued challenges of investing in Moldova. Targeted actions against strategic investors, politically connected individuals who "acquire" profitable businesses, systemic corruption, and legislative obstacles all conspire to make Moldova a place for only the savviest of investors. The actions of certain elements of the GOM challenge our confidence in their willingness to consolidate reforms, causing us to pause (even more than before) when counseling potential American investors about investing in Moldova. END SUMMARY.

"MOLDOVA: A NEW CHALLENGE AT THE EU'S BORDER"

¶12. (C) The GOM's awkwardly titled October 11-13 national investment forum is indicative of the investment climate in Moldova. As many investors note, one comes to Moldova (as with many emerging markets) because of the potential for high returns, understanding the challenges and risks. The GOM touts Moldova's comparative advantages as democratic stability, a legal framework which facilitates foreign investment, low-cost labor, favorable investment and tax incentives, and a strategic location between the EU and CIS (with preferential trade access to both markets). The GOM lauds its recent efforts to "liberalize" the economy: the adoption of a capital and fiscal amnesty, introduction of a zero tax rate for reinvested income, progress on privatizations, the creation of free economic zones, and plans to develop industrial parks.

INVEST IN MOLDOVA - AT YOUR OWN RISK

¶13. (C) Although the GOM has continued reforming Moldova's economy, the business and investment climate remains weak and hindered by corruption, excessive bureaucracy and a weak judicial system. For example, Union Fenosa, the Spanish owner of three power distribution companies, has been battling the GOM for over 10 months in response to the unilateral adoption of politically motivated tariffs for electricity which threaten the viability of the company's investment in Moldova. Union Fenosa tried to disconnect service to MoldCarton, a Russian-owned company close to the Moldovan leadership, because of non-payment of debts. Government officials, including the Prime Minister, would not

allow Union Fenosa to stop providing electricity to MoldCarton and pressured the company to accept a payment schedule favorable to MoldCarton.

¶4. (C) Other examples include the use of the Center for Combating Crime and Economic Corruption by politically connected local "investors" and elements of the GOM to take over or undermine profitable businesses. The allegations and outcomes of these investigations are rarely made public. Some new and disturbing challenges come from the recently established National Agency for the Protection of Competition, which has gone after France Telecom's Orange (mobile telephony) and Moldovan-American joint venture Sun Communications (cable television and internet provider) citing monopolistic practices. Both Orange and Sun are challenging domestic Moldovan competitors, who seem to be resorting to political interference to tilt the playing field in their favor.

¶5. (C) Government interference in the economy takes many forms - from unpublished internal decrees to government decisions which skirt legality. In the past year, we've seen examples of the GOM opaquely banning U.S poultry imports, adopting new regulations on non-alcoholic bottled beverages which hinder trade, and holding flawed tender offers for government procurements. Although the "Guillotine" process (reform of regulatory activity affecting businesses) was implemented successfully, and a second phase is underway, companies continue to note regulatory-type constraints (and related corruption) as impediments to their development.

NOT ALL PROBLEMS ARE STRUCTURAL

¶6. (C) Reforms and technical assistance will not resolve the
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problem of politically connected individuals who acquire profitable businesses through intimidation. According to anecdotal evidence, one of the worst offenders is Oleg Voronin, the son of President Vladimir Voronin. It is widely believed that Oleg, President of FinComBank, has acquired numerous businesses through intimidation and use of his family name. So abundant are the rumors that Oleg Voronin gave a rare interview in March 2007 (only his second public interview) to VIP magazine, a local publication, discrediting these charges and criticizing those who, for political reasons, go after the President's son. However, stories abound about the Voronin clan and their holdings. (NOTE: Recently, a CIS publication listed Oleg Voronin as one of the richest men in Moldova, claiming he was worth USD one billion. We doubt all his riches are the product of his business acumen. END NOTE.)

COMMENT

¶7. (C) Moldova has made efforts to improve its business and investment climate, with considerable support from the U.S. and other donors. Our MCC Threshold Country Program is an important effort in addressing one of Moldova's principle constraints to economic growth - corruption. Some GOM officials (such as, for example, First Deputy Prime Minister Greceanii and Minister of Economy Dodon) recognize that improving the investment climate is Moldova's key to a more prosperous future and seek to improve that climate. In addition, Parliamentary Speaker Marian Lupu often sides with those seeking to improve the business climate.

¶8. (C) Moldova's post-Soviet transition has been uneven. At times this country appears to have only a veneer of reform, although more than 15 years have passed since its independence. Moldova has enacted many new, progressive laws, but implementing and enforcing them will be the measure of true reform. Unless Moldova can improve the investment climate, it risks losing out to other low-cost competitors in

the region, becoming a haven only for Russian or other investors who do not care to operate under western norms.
KIRBY